

***United States Court of Appeals
for the Second Circuit***



**INTERVENOR'S
BRIEF**

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

United States Court of Appeals
for the District of Columbia Circuit

Docket No. 77-1547

FILED FEB 16 1978

BRADFORD NATIONAL CLEARING CORPORATION AND
BRADFORD SECURITIES PROCESSING SERVICES, INC.,

GEORGE A. FISHER
CLERK

Petitioners,

—against—

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

NATIONAL SECURITIES CLEARING
CORPORATION,

Intervenor
in support of
Respondent.

BRIEF OF NATIONAL SECURITIES CLEARING CORPORATION INTERVENOR IN SUPPORT OF RESPONDENT

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CERTIFICATE REQUIRED BY RULE 8(C) OF THE GENERAL RULES OF THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

The undersigned, counsel of record for National Securities Clearing Corporation, certifies that the following listed parties appeared below:

Bradford National Clearing Corporation	(for Petitioners)
Bradford Securities Processing Services, Inc.	(for Petitioners)

National Securities Clearing

Corporation

(for Respondent)

TAD Depository Corporation

(for Petitioners)

These representations are made in order that Judges of this Court, *inter alia*, may evaluate possible disqualification or recusal.

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BRIEF OF NATIONAL SECURITIES CLEARING CORPORATION INTERVENOR IN SUPPORT OF RESPONDENT

In this proceeding Bradford National Clearing Corporation ("BNCC") and Bradford Securities Processing Services, Inc. ("BSPS," and jointly with BNCC, "Bradford") seek to set aside an order, dated April 21, 1977, of the Securities and Exchange Commission (the "Commission"), which approved two rule changes submitted to it by National Securities Clearing Corporation ("NSCC") pursuant to section 19(b) of the Securities Exchange Act of 1934 (the "Act") as amended by

the Securities Acts Amendments of 1975 (the "1975 Amendments").¹ Although the named respondent in this proceeding is the Commission, NSCC is the party whose interests are directly affected.

COUNTERSTATEMENT OF THE CASE

1. Introduction

The asserted grounds for Bradford's challenge to the Commission's order approving NSCC's rule changes are that the rule changes will impose inappropriate burdens on competition and that the Commission's action approving them is inconsistent with its prior Order, dated January 13, 1977, granting NSCC's registration as a clearing agency (the "Order granting registration") (A. 1-36)². The fact is that the rule changes implement conditions that were imposed on NSCC by the Order granting registration so as to avoid potential burdens on competition and facilitate the establishment of an efficient national system for the clearance and settlement of securities transactions pursuant to the 1975 Amendments.

Bradford's assertions as to the anticompetitive consequences of the rule changes are in substance repetitions of the arguments it has made in *Bradford National Clearing Corp. v. SEC*, No. 77-1199 (D.C. Cir., filed February 16, 1977), currently pending in this Court, in which Bradford has challenged the Order granting registration ("*Bradford I*"). These arguments were also raised and considered by the Commission during the extensive proceedings that led to the Order granting registration. By repeating these arguments here, Bradford is thus again attacking the Commission's original action approving NSCC's registration. Since there is no need for this Court

¹ The Act, § 19(b), 15 U.S.C. § 78s(b) (Supp. 1977), as amended by the 1975 Amendments, Pub. L. No. 94-29, § 16, 89 Stat. 146.

² References in the form "A. " are to pages in the Appendix in this proceeding. References in the form "Br. " are to pages in Bradford's brief in this proceeding.

to consider the same issues involving the same parties twice, the Court in this proceeding should limit its review to the question whether the NSCC rule changes are consistent with the Order granting registration.

To accomplish even this limited review, however, it is necessary to understand the nature and the relationship of the parties, the issues that were considered in the proceeding that led to the Order granting NSCC's registration, the basic terms of that Order as it relates to the rule changes under review, as well as the nature and effects of the rule changes themselves and their relationship both to competition among clearing agencies and to the plan to establish, pursuant to the mandate of the 1975 Amendments, a safe and efficient national system for the clearance and settlement of securities transactions. We will therefore structure our presentation so as to present to the Court the facts and circumstances material to these matters (including the real, pro-competitive effects the rule changes have as opposed to the adverse consequences portrayed by Bradford), rather than employing the order of presentation adopted by Bradford in their brief for each of their many assertions.

2. The Parties

NSCC was incorporated on March 19, 1976 for the purpose of providing services to clear and settle securities transactions for its participants, which are principally brokers and dealers that are members of the American Stock Exchange, Inc. ("AMEX"), the National Association of Securities Dealers, Inc. ("NASD"), the New York Stock Exchange, Inc. ("NYSE"), or institutions such as banks and trust companies. The development of NSCC was the culmination of efforts by the broker-dealer community, in consultation with AMEX, NASD and NYSE, directed toward the establishment of a national clearing system and avoidance of the reoccurrence of the "paperwork crisis" that led to the liquidation of more than 100 brokerage firms in the late 1960's (A. 2-3).

Although NSCC is owned by subsidiaries of AMEX, NASD and NYSE, NSCC has been structured so that it will always be controlled by representatives of its broker-dealer and other participants, who serve on its board of directors on a rotating basis. NSCC is intended to operate for the benefit of its participants as a cooperative venture for the comparison, clearance and settlement of securities transactions with a view to lowering existing charges and refunding excess revenues.

On March 29, 1976, NSCC applied to the Commission for registration as a clearing agency pursuant to sections 17A and 19 of the Act. On January 13, 1977, after extensive proceedings, the Commission granted NSCC's application. Subsequent to the Order granting registration, the businesses of the American Stock Exchange Clearing Corporation ("ASECC"), the National Clearing Corporation ("NCC") and the Stock Clearing Corporation ("SCC"), subsidiaries of AMEX, NASD and NYSE, respectively, and sole shareholders of NSCC, were transferred to divisions of NSCC bearing the same names.

BNCC and BSPS are wholly-owned subsidiaries of Bradford National Corporation. Bradford National Corporation is a holding company listed on the American Stock Exchange which, in addition to its ownership of BNCC and BSPS, controls directly or indirectly certain banks, computer facilities and transfer service entities. Commencing in 1974, BNCC performed operational services for NCC pursuant to a facilities management contract. In January, 1977, NCC's business was transferred to the NCC Division of NSCC, and since that time BNCC has continued to act as facilities manager for the NCC Division under the 1974 contract. BNCC is also the facilities manager of the Pacific Clearing Corporation, one of NSCC's major competitors.

BSPS is a limited service clearing agency specializing in the receipt and delivery of municipal bonds. Its customers are principally commercial banks and municipal bond dealers. BSPS "picks-up" physical certificates from its customers and

delivers them pursuant to their instructions and collects payment therefor.

3. The Order Granting NSCC's Registration as a Clearing Agency

After receipt of NSCC's application for registration as a clearing agency, the Commission published formal notice thereof, invited "interested persons" to submit their views and announced that it would conduct public hearings on the application. The Commission specifically requested public comment on the justifications offered for NSCC's application and the effect of its registration as a clearing agency on competition among brokers and dealers and among clearing agencies. Public hearings on NSCC's application were held in June, 1976, during which twenty-three witnesses representing brokers and dealers, stock exchanges, clearing agencies, securities depository corporations, financial institutions and the investing public appeared to comment on all aspects of the proposed registration, especially its ramifications with regard to competition which were a central focus of the Commission's deliberations.

During the course of the public hearings and by means of the written comments submitted, the Commission was presented with detailed and conflicting analyses of numerous aspects of NSCC's registration, including most of the arguments regarding competitive issues set forth again by Bradford in its latest brief. Full argument was presented with regard to the effect of NSCC's registration on competition among brokers and dealers and among clearing agencies.³

³ BNCC and BSPS chose not to participate or to submit written comments opposing NSCC's application during this period and did not express any position on NSCC's registration prior to November 17, 1976 when, on the basis of similar arguments to those made by Bradford here, BSPS requested the Commission to impose certain restrictions on NSCC's registration for the exclusive benefit of BSPS, which the Commission declined to do (See NSCC Br. in *Bradford I* at 16).

On November 3, 1976, the Commission announced that it was considering approval of NSCC's application subject to four conditions, which the Commission believed would encourage development of an efficient, interfaced national clearing system that would promote competition among broker-dealers while creating an environment in which competition among clearing agencies would be free to develop. The Commission, in its release, requested public comments on the proposed conditions, which it received through November 19, 1976.

On January 13, 1977, after careful analysis of the extensive comments and the testimony concerning NSCC's registration, the Commission issued its Order granting registration on the basis of four conditions substantially similar to those set forth in the Commission's November 3rd release. Pursuant to the Order, the integration of the services previously offered by ASECC, NCC and SCC within the single entity of NSCC is to occur in two phases. During Phase I, ASECC, NCC and SCC are each to continue to operate as separate divisions of NSCC, and no changes may be made in the rules, operating procedures or facilities management arrangements of such divisions without the Commission's prior approval (A. 9, 25). Phase I is to continue until NSCC has satisfied the four conditions of the Order, at which time Phase II may commence and the services of NSCC's three divisions will be integrated into a single, more efficient operation.⁴

The condition in the Order granting registration that is most relevant to the present petition by Bradford is the "Free

⁴ The Order granting registration states that the Commission intended "to monitor closely the effects" of such Order and that "NSCC will operate in the context of continuing oversight conducted by the Commission" (A. 23, 24). In an exercise of this power, on January 15, 1978, the Commission gave notice of public hearings to begin on March 7, 1978, among other things "to examine the progress that has been made toward satisfaction of the conditions to NSCC's registration, whether the conditions are having their intended effect, and whether modifications to the Commission's Order and the conditions contained therein may be necessary." The Act Release No. 14411 at 4 (January 25, 1978).

Interface" condition, under which NSCC is required to establish "full interfaces" with the New York Clearing Corporation ("MCC"), the Pacific Clearing Corporation ("PCC") and the Stock Clearing Corporation of Philadelphia ("SCCP"), without interface charges, before commencing integrated Phase II operations (A. 25). The Commission defined a full interface as one through which any participant in either of the interfacing clearing corporations could move all its transactions in issues eligible for clearing and settlement at both clearing corporations (A. 31 n.121).⁵

4. Bradford's Prior Petition for Review of the Order Granting NSCC's Registration

On February 16, 1977, Bradford filed its petition in *Bradford I*, seeking review in this Court of the Order granting registration. In that petition, Bradford reargued the objections they had raised by letter to the Commission and which the Commission had considered prior to the issuance of the Order granting registration.⁶ In their present petition Bradford seeks to raise yet again certain of these issues—specifically those relating to the effect of NSCC's registration on competition, the requirement that BPS develop a system of continuous net settlement ("CNS") before it is eligible to participate in the

⁵ No interface was required with BPS because BPS lacks a netting system capable of interfacing with the systems of NSCC and these other clearing agencies. BPS has in its own words only "the most rudimentary mechanism" of picking up, transporting and delivering physical certificates and "requiring the broker to make separate payments on delivery for each trade" (Br. 3,9). As summarized in the record below, the question of a BPS interface, which the Commission resolved in the registration proceeding, presented "a three-prong hole and a two-prong plug problem" (A. 118). No interface is required until BPS establishes a system that would make "the prongs and the holes match" (*id.*).

⁶ See note 3, *supra*.

interface system,⁷ and the legality and effect of the so-called "tying" rules of NYSE and AMEX which are the subject of another proceeding pending before the Commission.⁸ The petition for review of the Order granting registration remains pending before this Court and, pursuant to this Court's order dated January 13, 1978, argument in that case will be heard on the same date and before the same panel as argument in the instant case.

5. The Order Approving NSCC's Rule Changes

On February 22, 1977, NSCC submitted to the Commission, pursuant to Rule 19b-4 of the Act and in compliance with the Order granting registration, the proposed Bond and Special Representative rule changes. The Commission thereupon gave public notice of the proposed rule changes and invited public comment. Only three letters of comment, from BNCC, BSPS and TAD Depository Corporation, another affiliate of Bradford National Corporation, were received during the comment period. These letters opposed the rule changes and requested a

⁷ See note 5, *supra*.

⁸ Bradford contends both in this proceeding (Br. 5-6, 10, 22, 33, 35, 56-57) and in *Bradford I* (see Bradford's Br. in *Bradford I* at 23-24, 44-45) that NYSE and AMEX have rules requiring trades executed in their markets to be cleared and settled through NSCC as the successor to their respective affiliated clearing agencies, SCC and ASECC. Both rules, however, contain an exception permitting members, at their election, to clear and settle their exchange transactions through other clearing agencies or otherwise and these rules are the subject of a separate proceeding before the Commission commenced on December 1, 1976 in which the Commission has stated it "expects that any amendments necessary to bring the AMEX and NYSE rules into conformity with the securities processing provisions of the Act will be made" before NSCC begins Phase II integrated operations (See NSCC Br. in *Bradford I* at 29-30). Both NYSE and AMEX have since filed proposed rule changes with the Commission that remove any remaining "tying" feature of the present rules. 42 Fed. Reg. 63979-81 (1977); S.E.C. Form 19b-4A of AMEX, dated November 11, 1977 (S.E.C. File No. SR-Amex-77-31).

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hearing pursuant to section 19(b)(2) of the Act to determine whether the rule changes should be disapproved.⁹

At the conclusion of the extended period for public comment, the Commission's staff prepared a memorandum analyzing the issues raised by Bradford and TAD Depository Corporation and, in reviewing this memorandum, the Commission considered the Bradford and TAD Depository Corporation arguments concerning the rule changes as well as whether these changes were in conformity with the Act and the Order granting NSCC's registration. As a result of its analysis, the Commission concluded, pursuant to the authority granted to it by section 19(b)(2) of the Act, that a public hearing on the rule changes was not justified.

On April 21, 1977, the Commission held an open meeting during which it considered the proposed NSCC rule changes (for the transcript of this meeting, see A. 106-19). At the meeting an Associate Director of the Division of Market Regulation of the Commission was questioned concerning the ramifications of the changes, specifically their effects on competition in general and on Bradford in particular. Following this discussion, the rule changes were approved by Order of the Commission dated April 21, 1977 (A. 120-25).

SUMMARY OF ARGUMENT

The Bond and Special Representative rule changes implement provisions of the Order granting registration that were adopted by the Commission both to carry out important statutory objectives and to respond to competitive concerns that had been raised by other clearing agencies in the proceedings leading up to that Order. Such rule changes, which enhance rather than injure the competitive positions of other clearing

⁹ A fourth letter of comment from BSPS was received after the expiration of the comment period but was considered by the Commission during a one week extension period for considering public comment granted by NSCC.

agencies, are wholly consistent with the Order granting registration and were properly approved by the Commission. The Commission, which was not required to reexamine issues that were fully reviewed in the Order granting registration, nevertheless gave due consideration to the objections raised by Bradford in their letters of comment, and the Commission's Order approving the rule changes contains a wholly adequate statement of its reasons for such approval.

POINT I

THE NSCC RULE CHANGES WERE APPROPRIATE TO SATISFY THE CONDITIONS IN AND WERE CONSISTENT WITH THE ORDER GRANTING NSCC'S REGISTRATION

A. The Bond Rule Change

Under the interface condition contained in the Order granting NSCC's registration, NSCC is required to establish, prior to commencing Phase II operations, full clearing interfaces with those clearing agencies that operate CNS systems (A. 15, 25). The interface condition was imposed by the Commission in response to the competitive concerns raised during the NSCC registration proceedings by the clearing agencies located outside New York City and in order to carry out the objectives of Congress in the 1975 Amendments of linking clearing and settlement systems, fostering cooperation and coordination among persons engaged in the clearance and settlement of securities transactions, and facilitating the establishment of a national clearing and settlement system (A. 14-15). Within a system of interfaces between NSCC and other clearing agencies having CNS operations, a broker may choose to be a member of only one clearing agency, which would be able to offer its participants clearance and settlement services with respect to any issue included in the national system, thus promoting competition among clearing agencies for the broker's business. This contrasts sharply with a system without interfaces in which the broker must clear and settle trades in

each marketplace through the clearing agency affiliated with that marketplace, which in effect requires brokers to become members of all clearing agencies and precludes direct competition among clearing agencies. Thus, the interface condition facilitates both competition among clearing agencies and the establishment of an efficient national clearing and settlement system.

The interface condition of the Order granting registration specifies that NSCC must establish full interfaces with MCC, PCC and SCCP as a prerequisite to entering Phase II. A "full interface" means that the link between the interfaced clearing agencies must be capable of handling transactions in all issues eligible in the clearing systems of both agencies (A. 31 n. 121). At the time of NSCC's registration, partial interfaces for listed securities were in effect with MCC, PCC and SCCP through the ASECC-SCC Regional Interface Operation. These interfaces, however, did not include debt issues listed on AMEX and NYSE. Therefore, since the interface condition mandates full interfaces capable of clearing and settling all securities transactions, NSCC was required to add debt issues to the interface system. There were two ways in which this could have been accomplished: (i) by NSCC modifying two existing systems, one in NSCC's ASECC Division for AMEX listed debt issues and one in its SCC Division for NYSE listed debt issues, to permit such securities to be included in the interfaces with MCC, PCC and SCCP, or (ii) by NSCC establishing a single system which could handle both AMEX and NYSE debt issues. Rather than modify two systems, which would be operated under different rules and would soon have to be dismantled and folded into the unified system of Phase II, NSCC determined to establish a single, more efficient interface system which could be put into effect at an earlier date (and therefore expedite the satisfaction of the interface condition to the Order granting registration) and would not later have to be changed.

The Bond Rule Change, therefore, is a technical rule change which allows NSCC to accomplish the objective of a

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single system for the required interfaces by removing all debt securities listed from time to time on AMEX from the list of securities eligible for clearance through the ASECC Division and adding them to the list of securities eligible for clearance through the SCC Division (A. 38). In this way, NSCC can use its data processing capability to permit transactions in all NYSE and AMEX listed debt securities to be included in the existing interfaces between the SCC Division of NSCC and each of MCC, PCC and SCCP (A. 39-40).¹⁰

Bradford's arguments against the Bond Rule Change are so confused with its arguments against the conditions of NSCC's registration, which are not properly part of this proceeding (see Point II, *infra*), that it is difficult to determine the precise nature of Bradford's complaint. Nevertheless, it appears that Bradford is asserting that the Bond Rule Change will permit NSCC to take customers away from BPS and two entities with which BNCC has a facilities management contract, PCC and Pacific Securities Depository Trust Company ("PSDTC"), by allowing NSCC to offer clearance and settlement services that no other clearing agency can offer at this time (Br. 1-2, 8, 12, 22, 23, 30, 37, 55, 56-57). This competitive injury supposedly follows from the Bond Rule Change because, Bradford maintains, it allows NSCC to consolidate its oper-

¹⁰ Shortly after the Commission approved the rule changes, NSCC made listed debt securities eligible for the interfaces with MCC, PCC and SCCP. As a result, each of these entities may now offer to its participants services to clear and settle AMEX and NYSE listed debt issues in addition to such services for equity issues which had been offered previously. Bradford's assertions that "these interfaces have not yet been full (sic) established" and that NSCC is the only entity with a single integrated system offering clearance and settlement "for transactions in all debt securities listed on NYSE and AMEX" (Br. 23) are not supported by the record and are simply false.

ations prior to satisfaction of the conditions contained in the Order granting registration. In Bradford's words:

"If NSCC is allowed to 'creep' toward Phase II without significant progress being made toward satisfying the conditions, enormous competitive injury (sic) will be done to the other clearing agencies" (Br. 37).

In this respect the Bond Rule Change is said to be inconsistent with the Order granting NSCC's registration which Bradford reads as requiring "that the transition from Phase I to Phase II occur 'all at once'" (Br. 40).

Bradford's arguments are based either upon a complete misunderstanding or a deliberate misrepresentation of the purpose and effect of the Bond Rule Change. Contrary to Bradford's unsupported assertions, the Bond Rule Change is intended to enable NSCC to move toward satisfaction of the interface condition of the Order granting registration, a requirement for the commencement of Phase II, and its effect is to permit full, efficient interfaces between NSCC and MCC, PCC and SCCP, thus fostering competition among clearing agencies.

Bradford's charge that the Bond Rule Change permits NSCC to offer clearance and settlement services that no other clearing agency can offer (Br. 23) is, as noted (note 10, *supra*), simply false. Far from giving NSCC a monopoly position in the clearing industry, the Bond Rule Change heightens the potential for competition among clearing agencies. For example, with the inclusion of listed debt issues in the NSCC-PCC interface, PCC now can and does offer to its participants, most of which are brokers, dealers and institutions located on the West Coast, full clearance and settlement services with respect to most AMEX and NYSE listed equity and debt issues, over-the-counter ("OTC") issues and, of course, issues listed on the Pacific Stock Exchange ("PSE"). PCC's participants can thus, through a single account at PCC, clear and settle all of their securities transactions eligible for clearance at PCC without

Bond Rule allows interface w/ PCC MCC SCCP

having to use the clearance and settlement services of NSCC. As a result, PCC's clearance and settlement business (and, as a corollary, BNCC's profits as facilities manager for PCC) should increase rather than decrease. Presumably for that reason, PCC, MCC and SCCP have not opposed the rule change (A. 109).

Contrary to Bradford's argument, in fact, the Bond Rule Change allows interfacing clearing agencies to offer consolidated services that NSCC will not be able to offer until the commencement of Phase II. The basic change in NSCC's clearance and settlement operation that will occur at that time is the consolidation of OTC transactions into a single account with AMEX and NYSE listed transactions (A. 11, 24-25). At present, OTC transactions are cleared and settled in NSCC's NCC Division in a system operated for NSCC by BNCC, which acts as a facilities manager for the NCC Division. That system is materially different in both format and procedure from the system operated for NSCC by Securities Industry Automation Corporation ("SIAC"), facilities manager for the ASECC and SCC Divisions. No change in these two arrangements is contemplated by the rule changes. MCC, PCC and SCCP, however, are not subject to the limitations on combining listed and OTC clearing that are contained in the Order granting NSCC's registration. These other clearing agencies therefore are able to establish single account processing, which, as a result of the Bond Rule Change, may now be applied to all listed debt transactions as well as transactions in listed equity and OTC issues. Thus, contrary to Bradford's assertion, PCC, for example, currently offers services that NSCC is not yet permitted to offer, rather than vice versa.

Bradford also argues that NSCC is being allowed to "creep" toward Phase II and that a "fair reading" of the Order "makes clear that the Commission required that the transition from Phase I to Phase II occur 'all at once'" (Br. 40). This argument is untenable and unsupported by the language of the Order. The Order directs that NSCC may not begin operating

as an integrated system or, without prior Commission approval, make any changes in its rules or of the rules of any of its operating divisions "unless NSCC shall have first ... established full interfaces" with MCC, PCC and SCCP, among other conditions (A. 24-25). Thus, in plain English, the conditions, including the interface condition, must be satisfied "first" before integration of the listed ASECC and SCC systems with the NCC Division's OTC system. Furthermore, rule changes during the interim period are explicitly permitted, provided that prior Commission approval is obtained, as it has been in this instance. It is ludicrous to argue, as Bradford has done here, that to take a step in the direction of complying with one of the conditions to the Order granting registration is invalid because it "creeps" to Phase II, when the Order itself, which is not subject to review in this proceeding, specifically directs that such compliance is a prerequisite to entering Phase II. In short, the only "fair reading" of the Order is that rule changes, made with the approval of the Commission, that effectuate compliance with the stated conditions are to be encouraged. The Commission properly perceived this point when it stated in the Order under review here that "the proposed rules are consistent with the Order granting NSCC's registration" and "are designed to implement 'the Free Interface Condition'" (A. 122).

Nor is the Bond Rule Change inconsistent with the Order granting NSCC's registration merely because it permits all NYSE and AMEX debt securities to be cleared and settled in a single interface system. Although Bradford characterizes this element of the change as a "*de facto* integration of the bond operation of the ASECC (sic) Division of NSCC with that of the SCC Division of NSCC" (Br. 30), Bradford fails to indicate that the entire clearing and settlement operation of these entities was combined many years ago, long prior to the Order granting NSCC's registration. In the Order granting registration the Commission found, for example, that "ASECC and SCC and their combined operations, which are run by SIAC,

provide participants with prompt and accurate service" (A. 13). The Commission also made repeated references in the Order granting registration to the single "ASECC-SCC system" (e.g., A.13) and noted that "under existing arrangements participants in ASECC and SCC may make one daily money settlement for obligations to the two clearing corporations" (A. 32 n.128). Accordingly, ~~no substantial change in the operation of NSCC's ASECC and SCC Divisions was made or contemplated by the Bond Rule Change (see A. 9).~~

With this background in mind, it is readily apparent that the Order granting registration was never intended to require the establishment of interfaces utilizing duplicative systems which would only have to be discontinued at the outset of Phase II. Instead, the Order anticipated a combined "ASECC—SCC Regional Interface Operation" during Phase I (A. 15). Indeed, one of the major advantages the Commission found in NSCC's application ~~was the avoidance of duplicate facilities that would "delay the attainment of important objectives of the Act by * * * impeding the linking of clearing systems by requiring other clearing agencies to establish interfaces with two clearing systems, rather than one"~~ (A. 18; see also A. 22).

Despite the Bond Rule's complete compliance with the Order granting registration, Bradford tries to manufacture an issue of competitive injury to itself. The invalidity of this argument in regard to BNCC becomes manifest upon realization that the Bond Rule Change will have absolutely no effect on BNCC's present position in the clearance and settlement of OTC transactions for NSCC. As noted, such transactions, which are not affected by the Bond Rule Change, are cleared and settled in a system operated by BNCC as facilities manager for NSCC. BNCC, moreover, as stated previously, is the facilities manager for PCC and since PCC's competitive position is improved by the Bond Rule Change, BNCC will be the gratuitous beneficiary of such improvement.

As regards BSPS, a close reading of Bradford's brief reveals that the root of its claim of competitive injury is the inescapable fact that BSPS has not developed a CNS system and therefore has not been able to participate in the interfaced system. BSPS's own filings with the Commission state that BSPS provides only a "pick-up" and delivery service, which is used primarily for "municipal securities".¹¹ At one point in its brief, BSPS thus admits that it offers only "the most rudimentary mechanism" of picking up, transporting and delivering physical certificates (Br. 3, 9). Although Bradford states that on August 24, 1977 BSPS mailed a Form 19b-4A to the Commission as the first step in developing and establishing a full clearance and settlement system for all securities (Br. 11), BSPS's real intentions remain unclear. In its Form 19b-4A, BSPS still does not propose to establish a CNS system, which is a precondition to BSPS's participation in the system of interfaces required to be implemented by NSCC under the Order granting registration (A. 15). Moreover, BSPS hedges (Br. 20 n. 11) concerning its intentions, using as an excuse for not establishing a modern clearing system the illogical assertion that it is prevented from doing so by the Special Representative Rule Change (see Point I(B), *infra*).

To whatever extent the rule changes make the services offered by NSCC, MCC, PCC and SCCP more attractive than those offered by BSPS, it is solely because BSPS has failed to develop a modern CNS system of clearance and settlement and not because of any asserted anticompetitive restraints. Competition among clearing agencies that are seriously in the business of providing clearance and settlement services is enhanced rather than hindered by the rule changes, and it is BSPS's lack of capacity to interface with these other clearing agencies that is the source of its claim of injury. Should BSPS develop an interface capability in the future, it will of course be able to compete with NSCC, just as PCC is able to do under the

¹¹ S.E.C. Form CA-1 of BSPS, dated November 20, 1975 (S.E.C. File No. 600-2).

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B trying to prevent competition from other CC's besides NSCC

Bond Rule Change (see *supra*). But BSPS should not be protected forever in its use of an antiquated operation. By their attempt in this proceeding to prevent NSCC from including listed debt securities in its interfaces with MCC, PCC and SCCP, Bradford seeks only to insulate BSPS from competition by other clearing agencies offering more technologically advanced services to users than BSPS currently provides. BSPS should concentrate on upgrading its operations so that it may participate in a modern system, rather than impeding progress by all clearing agencies through obstruction and delaying tactics.¹² The Commission has properly balanced broad public interests in facilitating the establishment of a safe, efficient, national clearing system and the creation of a competitive environment for brokers, dealers and clearing agencies, while refusing to impede these public interests by allowing special protections in the form of the indefinitely extended delays that BSPS has requested. Quoting Donald Baker (then Assistant Attorney General, Antitrust Division, of the Justice Department), the Commission has properly recognized that "preserva-

¹² In addition to its attempt here to prevent NSCC from including listed debt securities in its interfaces, since October, 1977 BNCC, as facilities manager for NSCC's NCC Division, has refused to implement systems changes required to establish interfaces for OTC transactions with MCC and SCCP in compliance with the full interface condition of the Order granting registration. After repeated requests by NSCC, BNCC recently stated it would make the changes provided it is guaranteed compensation (to which it is not entitled under the facilities management contract) for any loss of revenue it may suffer as facilities manager occasioned by broker-dealers, who previously cleared and settled their OTC transactions through the NCC Division of NSCC, electing to clear and settle such transactions through MCC or SCCP. In addition to demonstrating its interest in obstruction and delay, BNCC's recent demand for compensation furnishes dramatic support for NSCC's position here that adding securities to its interfaces with PCC, MCC and SCCP *improves* the competitive positions of such clearing agencies at the expense of NSCC.

tion of competition should not be confused with preservation of a particular competitor" (A. 115).¹³

B. The Special Representative Rule Change

In addition to requiring that listed bonds be included in the interface system, the full interface condition was designed to facilitate at the initiation of NSCC's Phase II operations a national system of interfaced clearing agencies whose participants may compare, clear and settle their transactions in securities eligible in the system without having to become a member of more than one clearing agency (A. 6, 15, 25, 31 n. 121). In the words used in the Order granting NSCC's registration, "a participant should be able to obtain one account processing through one clearing entity" (A. 6). Stated in simplest terms, the Special Representative Rule Change assists in meeting this objective by permitting a purchaser or seller of securities, who may be a participant in a clearing agency having an interface with NSCC, access through an intermediary (the Special Representative) to the facilities of NSCC for purposes of clearance and settlement of his trade, without such purchaser or seller having to become a member of NSCC.

To demonstrate how the Special Representative Rule Change facilitates implementation of the full interface condition, it is necessary to explain the comparison, clearance and settlement operations of a regional broker before and after the Rule Change, which are best understood in the context of specific examples.

Assume therefore that a broker in Los Angeles, which is not a member of NYSE and has no offices in New York, wants to purchase securities listed on NYSE on behalf of its customer, a bank also located in Los Angeles. In order to effect the trade on NYSE, the Los Angeles broker will have to use a "corre-

¹³ As stated by the Fifth Circuit Court of Appeals: "We will not reject an administrative decision merely because one producer's piece of cake is iced and another's is not." *Placid Oil Co. v. F.P.C.*, 483 F.2d 880, 905 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp. v. F.P.C.*, 417 U.S. 283 (1974).

spondent" broker that is a member of NYSE, which will execute the trade on the floor of the exchange. Prior to the Rule Change, the correspondent broker would submit data concerning the terms of the trade to NSCC for comparison with similar data submitted by a broker on the other (or "contra") side of the trade. NSCC would compare the data and if it matched would record a "compared trade" between the correspondent broker and the contra broker. On the fifth business day after the trade occurred, the correspondent broker would receive the securities purchased and make payment therefor to NSCC, which would be the end of NSCC's role in settling the transaction. The correspondent broker would then have to make its own arrangements for delivery of the securities to and collection of payment from the Los Angeles broker, which in turn would have to make similar arrangements with the Los Angeles bank. The inefficiencies involved in this system and the competitive handicap on the Los Angeles broker as opposed, for example, to a New York broker having membership in NYSE and NSCC, are obvious. Even if the Los Angeles broker were a full clearing member of PCC, PCC's facilities could not be used to clear and settle the transaction between the broker and its correspondent unless the correspondent was also a member of PCC.

With the implementation of the Special Representative Rule Change, the Los Angeles broker has the option of having its correspondent broker, a member of NSCC, act as its Special Representative. Under this system the correspondent broker reports data relating to three "sides" to NSCC: (i) the purchase of securities on NYSE by the correspondent, which must be compared with data submitted by the contra broker; (ii) a "sale" of the same securities by the correspondent to the Los Angeles broker, and (iii) a "purchase" of the same securities from the correspondent by the Los Angeles broker, which is indicated to be a member of a clearing corporation having a full interface with NSCC, in this instance, PCC. NSCC would record an identical purchase, side (i), and sale, side (ii), by the correspondent broker. Appropriate debit and credit entries would also be made between NSCC and PCC. As a result,

when each of the transactions is completed, and the entries at NSCC and PCC are made, the positions of the correspondent broker will net to zero. On the settlement day, NSCC would receive securities from the contra broker and deliver securities via the interface to PCC, which in turn would deliver them to the Los Angeles broker. Similarly, NSCC would make payment to the contra broker for the securities delivered and receive payment from PCC, which in turn would receive payment from the Los Angeles broker. All of the Los Angeles broker's transactions would be netted in its single account at PCC with one daily money settlement covering all activity in the account and one settlement in each issue traded that day. PCC and the Los Angeles broker would thus both benefit from the increased use of the interface system without either having to be a member of NSCC, thus promoting competition between broker-dealers and between clearing agencies.

Another objective of the Order granting registration and the 1975 Amendments was to provide "financial institutions" as well as brokers and dealers with direct or indirect access to modern clearance and settlement facilities (A. 5). The Commission has defined "financial institutions" to include "banks, insurance companies, investment companies, clearing agencies and any other entities which receive, deliver or hold securities" (A. 28 n. 53). Where brokers execute transactions on behalf of customers, rather than acting as principals, for each broker-to-broker transaction there are two customer side transactions. The intention of the 1975 Amendments and the Order granting registration was to facilitate the establishment of means by which customer side transactions of this type could be included in the national clearing system, thereby making them eligible for the benefits of book-entry transfer of securities and netting.

The Special Representative Rule Change facilitates achievement of this objective. Again, this is best understood in the context of a specific example. To take the simplest case, assume that a broker in New York executes a sale of securities on NYSE on behalf of an institutional customer. The broker submits the trade data to NSCC for comparison with data

submitted by the contra broker. If comparison is effected, the broker will have an obligation to deliver the securities on the settlement date and will receive payment therefor from NSCC. Prior to the Rule Change, the broker had to arrange to receive the securities and to make payment to the institutional customer outside of NSCC's system. If the broker and the customer were both members of The Depository Trust Company ("DTC"), a depository which maintains custody of securities in book-entry form, the customer transaction could be completed by the broker and the institution instructing DTC to make a book-entry movement of the securities in question from the account of the institution to the account of the broker and also to debit the broker's cash account and credit the institution's cash account at DTC. Thus, without the Rule Change, the broker would have a credit in its cash account at NSCC and a debit in its cash account at DTC. If this were the broker's only transaction that day, the broker would receive a check from NSCC and issue a check in the same amount to DTC.

The Rule Change permits DTC, acting as a Special Representative, to submit to NSCC the two "sides" of the customer transaction: (i) the "sale" of the securities by the institution, and (ii) the "purchase" of the securities by the broker. The institution would then have an obligation to deliver the securities on the settlement date and would receive payment therefor directly from NSCC. The broker's "purchase" of the securities from its customer would net out against its sale of the same securities to the contra broker, thus leaving the broker with no net securities settlement obligation.

As the example illustrates, the Special Representative Rule Change permits settlement of delivery and payment obligations between the ultimate seller and the ultimate purchaser, thus eliminating the intermediate securities settlements between the ultimate seller and its broker, its broker and the contra broker, and the contra broker and the ultimate purchaser. Moreover, where the Special Representative is a depository associated with an interfaced regional clearing agency, the Rule Change also permits settlement directly between customers in different

parts of the country through the interface system. For example, the customer making the sale could settle with NSCC, the customer making the purchase could settle with PCC, and the clearing agencies would settle through the NSCC-PCC interface. In this manner, institutions throughout the country can benefit from increased safety and efficiency resulting from the clearing agencies' trade guarantees and netting processes and regional clearing agencies can benefit from the expanded use of the interface system.

Bradford attacks the Special Representative Rule Change on the ground that it eliminates the traditional comparison function of clearing agencies (Br. 50-51), and thus "will limit BSPS's ability to offer its comparison and settlement service to present and prospective participants for trades in securities which are cleared by SCC and where the contra side is a Special Representative (Br. 11). In fact, as the examples given above illustrate, comparison of transactions executed on the floors of AMEX and NYSE (other than odd lots) between brokers who are members of those exchanges must still be performed by a clearing agency. The Special Representative Rule Change does not eliminate or reduce the necessity for this comparison nor does it reduce the necessity for comparison between a broker and its customer.

Bradford also objects to the inclusion in the national clearing system of financial institutions, smaller brokerage firms, and non-participants that are participants in one of the regional clearing agencies interfaced with NSCC (Br. 31-33). But here again Bradford's real objection is based on its lack of an interface, an issue which was fully considered and properly resolved by the Order granting registration, which is subject to review in a separate proceeding (see Point II, *infra*). Indeed, Bradford concedes "the ultimate desirability" of opening direct participation in the national clearing system to a wider group of institutions, but argues only that this improvement in the system

should be delayed indefinitely so that BSPS, if it so chooses at some point in the future, may improve its system (Br. 31).¹⁴

Finally, Bradford argues that the Special Representative Rule Change compels the reporting to the SCC Division of all trades with non-participants in "acceptable" securities (Br. 33). Indeed, Bradford goes so far as to say that the Special Representative Rule Change will function as a rule "tying" the comparison function to NSCC, thus precluding BSPS from competing (Br. 20 n.11).

What Bradford chooses to ignore is that there is nothing mandatory about the Special Representative Rule. Brokers, whether NSCC members or not, and financial institutions can utilize this service or not as they choose. The Special Representative is a means of access to the national system. As the examples show, the Rule should increase the business of all interfaced clearing agencies and make them more competitive. Other interfaced clearing agencies, in addition, may and do offer their own version of the Special Representative Rule in order to improve still further their competitive positions. When BSPS says it is precluded from competing, it is in effect admitting that its rudimentary operation cannot compete with the modern clearance and settlement systems which were facilitated by the 1975 Amendments and the Order granting registration, developed by NSCC and the other interfaced clearing agencies, and partially implemented by effecting the rule changes here under review.

It is respectfully submitted that the Commission was entirely correct in stating:

"The Commission has reviewed the proposed rule changes and the comment letters received and has determined that the proposed rules are consistent

¹⁴ Here, as elsewhere, BSPS uses as excuses for not improving its system the so-called tying rules and the lack of an interface, which were shown by NSCC's brief in *Bradford I* to have no merit (see Point II (A), *infra*).

with the order granting NSCC's registration as a clearing agency and with the purposes of the Act. Both proposed rule changes are designed to implement 'The Free Interface Condition' to the order. The first submission would add transactions in Amex-listed debt securities to the transactions in NYSE- and Amex-listed equity securities and NYSE-listed debt securities which currently may be cleared through clearing agencies participating in the SCC Division's RIO interfaces. The second submission would enable a non-participant in NSCC who participates in a clearing agency interfaced with the SCC Division through RIO to clear and settle, through the interface, transactions in any security eligible for clearance through the SCC Division. *Instead of restricting competition among registered clearing agencies, the proposed rule change would allow broker-dealers a wider choice in clearance and settlement*" (Emphasis supplied) (A.122).

No inquiry by the Commission beyond that made in approving these rule changes and in granting NSCC's application for registration was required.

POINT II

THE COMMISSION SATISFIED ITS STATUTORY OBLIGATIONS BY FULLY CONSIDERING ALL THE ISSUES CONCERNING THE RULE CHANGES THAT WERE PROPERLY BEFORE IT

Under section 19(b)(2) of the Act, the Commission is required to "approve a proposed rule change of a self-regulatory organization if it finds that such proposed rule change is consistent with the requirements of [the Act] and the rules and regulations thereunder applicable to such organization." The Act, § 19(b), 15 U.S.C. § 78s(b) (1971 & Supp.

1977). Since the Commission had so recently and thoroughly interpreted the Act as it related to NSCC in the Order granting registration, the Commission's task in reviewing the proposed rule changes was limited essentially to a determination that, as demonstrated in Point I, *supra*, the rule changes are consistent with the prior Order. Moreover, the Commission's findings "that the proposed rules are consistent with the order granting NSCC's registration" (A. 122), if supported by substantial evidence, are unreviewable. The Act, § 25(a)(4), 15 U.S.C. § 78y(a)(4) (1971 & Supp. 1977); *Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 402, 416 (1971); *Ethyl Corp. v. E.P.A.*, 176 U.S. App. D.C. 373, 406, 541 F.2d 1, 34, *cert. denied*, 426 U.S. 941 (1976); *International Harvester v. Ruckelshaus*, 155 U.S. App. D.C. 411, 437, 478 F.2d 615, 641 (1973); *Archer v. S.E.C.*, 133 F.2d 795, 799 (8th Cir.), *cert. denied*, 319 U.S. 767 (1943).

As noted by the Commission in the Order granting registration, the Act "directs the Commission, in exercising its mandate to facilitate the establishment of a national clearing and settlement system, to perform [a] balancing function, 'having due regard for the public interest, the protection of investors, the safeguarding of securities and funds, and maintenance of fair competition among brokers and dealers, clearing agencies, and transfer agents . . . ' [the Act, § 17A(a)(2)]" (A. 5). The Commission thus found that it "must balance the maintenance of fair competition and a number of other equally important express purposes of the Act." *Id.*

Despite the clarity of the Act and the obvious correctness of the Commission's interpretation, Bradford devotes a substantial proportion of its brief to the argument that "the 1975 Amendments were 'designed to force the Commission to focus with particularity on the competitive implications of each regulatory requirement'" (Br. 14, 15, 29, 34-35, 43-44, 59). Finding no support for the argument in the Act itself, Bradford cites two inapposite bits of legislative history. The first (cited at

Br. 13) is from a ~~House Report~~¹⁵ accompanying a bill that never became law. The second quotation (cited at Br. 14, 29, 34, 35), from which Bradford draws the language of "particularized" evaluation, is from that portion of a Senate Report¹⁶ relating to the national market system rather than the national clearing system.

There is good reason for Bradford to omit reference to the portion of the Senate Report discussing the national clearing system, which has a decidedly different emphasis from the section that discusses a national market system. Competition was one of the primary concerns of the Senate Report's discussion of a national market system, whereas competition is not mentioned in the Report's discussion of the regulation of clearing agencies. Instead, the emphasis is on centralizing authority in the Commission to regulate these agencies "in a bold and effective manner to facilitate the rapid development of a nationwide system for processing securities transactions."¹⁷ It was this mandate that the Commission carried out in its Order granting NSCC's registration.

A. The Commission Was Not Required to Reexamine Issues That Were Fully Considered in the Order Granting NSCC's Registration

In the three letters Bradford submitted to the Commission opposing the rule changes (A. 93-103), the basic questions raised were ones that had been resolved by the Commission during the course of the proceedings to consider NSCC's registration and were briefed for this Court in Bradford's

¹⁵ House Comm. on Interstate and Foreign Commerce, Report to Accompany H.R. 4111, H.R. Rep. No. 94-123, 94th Cong., 1st Sess. (1975).

¹⁶ Senate Comm. on Banking, Housing and Urban Affairs, Report to Accompany S. 249, S. Rep. No. 94-75, 94th Cong., 1st Sess. 14 (1975). These misstatements by Bradford as to the relevant legislative history have been called to Bradford's attention previously (See the Committee's Br. in *Bradford I* at 50 n. 77; NSCC Br. in *Bradford I* at 42).

¹⁷ *Id.* 55.

appeal seeking review of the Order granting NSCC's registration. The arguments, which are again raised in Bradford's latest brief, are the following:

(i) NSCC was improperly granted a virtual monopoly in the clearing industry and its registration will have a "grossly anticompetitive impact on the clearing industry" (Br. 18; *see* Br. 5, 19, A.94);

(ii) BSPS is placed at a severe competitive disadvantage because it was improperly denied an interface with NSCC (A. 94, 95; Br. 17, 20, 26, 30, 33); and

(iii) The "tying" rules of NYSE and AMEX prevent BSPS from developing sufficient trade volume to compete effectively with NSCC or develop a CNS system (A. 101, 102; Br. 5-6, 10, 20, 22, 33, 35, 56-57).

These are Bradford's real complaints—an analysis of Bradford's brief shows that if these issues were resolved or decided against Bradford, Bradford's objections to the rule changes would evaporate.

Since these issues had been raised and resolved in the prior registration hearings, the Commission was not obligated to reexamine them in its consideration of NSCC's proposed rule changes. *Alabama Power Co. v. F.P.C.*, 167 U.S. App. D.C. 145, 511 F.2d 383 (1974); *Panhandle Eastern Pipe Line Co. v. F.P.C.*, 236 F.2d 606, 609, 612 (3d Cir. 1956). In the *Alabama Power* case this Court ruled:

"An agency may . . . keep its administrative burden manageable by refusing to engage in protracted reconsideration of a decision reached after thorough exploration of the matter in a prior rulemaking proceeding. It may, for example, limit reexamination of a particular matter to reasonable intervals, to insure that reconsideration occurs against an adequate background of experience, and to conserve

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administrative resources by providing interested parties an incentive to introduce in a single proceeding all information pertinent to the issues presented." 167 U.S. App. D.C. at 150-51, 511 F.2d at 388-89.

The statement by the Commission in the Order approving the rule changes that they are "consistent with the Order granting NSCC's registration" (A. 125) is the equivalent of a statement that it will not reconsider issues previously considered and ruled upon in the proceedings that led to the Order granting registration. This position is supported by the reasoning of the court in *T.S.C. Motor Freight Lines, Inc. v. United States*, 186 F. Supp. 777 (S.D. Texas 1960), *aff'd*, 366 U.S. 419 (1961), in which the court ruled:

"The Administrative Procedure Act does not require that detailed findings with supporting reasons previously made and adhered to by the Commission be reiterated after each attack. The statement by the Commission that the 'findings of the Commission [are] in accordance with the evidence and the applicable law' is obviously a statement that the Commission is standing behind the original detailed and articulate findings and conclusions. The law requires no more." 186 F. Supp. at 787.

In any event, Bradford's arguments are without merit for the reasons set forth in NSCC's brief in *Bradford I* (see, particularly, NSCC Br. in *Bradford I* at 21-30). As stated therein, NSCC's registration facilitates the prompt achievement of a national clearing system, will achieve the regulatory purposes of the 1975 Amendments and will increase competition among brokers and dealers as well as among clearing agencies. Contrary to Bradford's assertions, BPS has not been denied an interface with NSCC; rather, the Commission has directed NSCC to make available, and NSCC has offered, a "full interface" to BPS as soon as it develops a clearing system that has the capacity to have or would require an interface with

NSCC. And the so-called "tying" rules of NYSE and AMEX, which in any event contain exceptions permitting members of those exchanges to clear and settle their exchange transactions through other clearing agencies, are presently the subject of a separate Commission proceeding, and both NYSE and AMEX have filed proposed rule changes with the Commission that remove any remaining "tying" features of the kind objected to by Bradford (see note 8, *supra*).

B. The Commission Sufficiently Articulated Its Resolution of All Issues Concerning the Rule Changes That Were Properly Before It

As noted *supra* at 8-9, only four letters of comment were received by the Commission in regard to the rule changes—one from BNCC (A. 98-99), two from BPS (A. 93-97, 100-03) and one from TAD Depository Company (A. 91-92). The number of objections contained in these letters was limited. Bradford argues, however, that the Commission failed to articulate sufficiently the bases on which the Commission resolved these objections, which Bradford asserts is fatal to the Order regardless of the correctness of its conclusions.

Most of the objections raised by the letters were dealt with specifically in the Order approving the rule changes (A. 122-25). Of these, the principal objections involved allegations that NSCC was attempting to circumvent the interface condition of the Order granting registration by consolidating its services prior to the fulfillment of this condition and that the rule changes would adversely affect competition among clearing agencies, specifically the competitive position of BPS. The Commission devoted the bulk of its discussion of the rule changes during its open meeting of April 21, 1977 to these two considerations. These issues, together with all other issues raised by the letters of comment, had been analyzed by the Commission's staff prior to this meeting, but the Commission again questioned the staff to determine if it was satisfied that

the objections did not warrant disapproval of the rule changes. The conclusions of the staff, adopted by the Commission and incorporated in the Order, were that the rules facilitated the implementation of the interface condition and that the rules did not ~~restrict competition among clearing agencies but would allow broker-dealers a wider choice in clearance and settlement and hence advance competition~~ (A. 106, 109, 112, 115, 118, 122, 123). The Commission was cognizant of the fact that Bradford's disadvantage was in not having an interface with NSCC and that this interface would not be required pursuant to the Order granting registration until Bradford developed a CNS system (A. 111, 116, 117).

Only three issues were raised by Bradford in their letters of comment that were not specifically ruled upon in the Order approving the rule changes, and each of these was discussed at the Commission's open meeting. BSPS raised the issue of a proposed Depository Trust Company rule change that would restrict depository interfaces with it to non-profit organizations and to trust companies (A. 96-97), which the Commission correctly concluded was not properly before it in these proceedings (A. 117). BSPS further argued that the rule changes would force brokerage firms to become members of NSCC and withdraw from all other clearing agencies (A. 102). The Commission's staff, in response to questioning by the Commission, rejected this argument and noted the absence of any negative comment from the regional clearing agencies (who have not heretofore been reticent in protecting their interests¹⁸) (A. 109).¹⁹ Finally, BNCC requested that a decision on the rule changes be postponed until Bradford's proceeding in this Court to review the Order granting registration was decided for the reason that the rule changes would subvert the current NSCC divisional structure and thus render a decision in Bradford's

¹⁸ See, e.g., A. 15 and NSCC Br. in *Bradford I* at 14-15.

¹⁹ It should be noted that the rule changes have been in effect since April 21, 1977 without causing any of the untoward effects predicted by Bradford.

favor on its first appeal meaningless (A. 98). The Commission's staff, however, specifically noted that the rule changes did not involve an irrevocable step (A. 107).

Despite the Commission's consideration of each of the issues raised by Bradford and TAD Depository Corporation during the period for public comment on the proposed rule changes, Bradford now argues that the Commission's considerations were insufficient in that the Order did not specify each anticompetitive effect and provide analysis supporting a view that such effects were necessary or appropriate in furtherance of the purposes of the Act. In so arguing, Bradford misconceives the scope of the analysis that must be included in a Commission order approving rule changes, and utterly disregards the meticulous considerations that the Commission gave to substantially the same matters in the Order granting registration and during the proceedings that led to the adoption of that Order, all of which served as the backdrop for the Commission's Order approving the rule changes.

Pursuant to section 19(b)(2) of the Act, the Commission had either to enter an order approving the proposed rule changes as consistent with the requirements of the Act or institute proceedings to determine whether the rule changes should be disapproved. Despite requests by BPS for such a proceeding to disapprove, the Commission determined, as stated in the Order approving the rule changes, "that the proposed rules are consistent with the order granting NSCC's registration as a clearing agency and with the purposes of the Act" (A. 122). In so determining, the Commission was acting well within its range of statutory discretion.

Bradford would have this Court make the novel ruling that unless the Commission discussed in detail its analysis of the competitive arguments made by Bradford in opposition to the rule changes in either its open meeting or in this particular Order, the decision to approve the rule changes must be overturned. Such an argument is unsupportable as a matter of law.

The proceeding before the Commission in this case was not one that was required to be determined on the record after an agency hearing. The Act, § 19(b)(1), (2)(A), 15 U.S.C. § 78s(b)(1), (2)(A) (1971 & Supp. 1977). In such matters, section 23(c) of the Act, added by the 1975 Amendments, requires only that the Commission's Order "be accompanied by a statement of written reasons." The Act, § 23(c), 15 U.S.C. § 78w(c) (1971 & Supp. 1977). It was recognized by the Senate Committee, which recommended this procedure for the Commission's review of proposed rule changes by self-regulatory organizations, that in "most situations the SEC's statement would be purely perfunctory and might simply be an endorsement of the justification filed by the self-regulatory organization." Senate Rep. No. 94-75, *supra* at 30. In other words, the Commission may routinely adopt as its statement of written reasons under section 23(c) "~~the concise general statement of the basis and purpose of such proposed rule change~~" filed by the self-regulatory organization under section 19(b)(1). The Committee further stated that only rule changes "which would have significant policy implications" would require the Commission to issue its own statement of reasons. *Id.* Since, as shown above, the rule changes here under review were consistent with the Commission's prior Order granting registration (which contained a full and complete statement of reasons), they do not in fact raise any significant policy questions, but the Commission nevertheless clearly set forth in the Order approving the rule changes the reasons for its action. No more was required by the Act.

The courts in other contexts have similarly differentiated between agency proceedings required to be determined on the record after hearings and those not required to be so determined in terms of the detail required to be included in the record and the scope of the analysis required to be made by the agency. Thus, in *Mobil Oil Corp., v. F.P.C.*, 152 U.S. App. D.C. 119, 469 F.2d 130 (1972), *cert. denied*, 412 U.S. 931 (1973), petitioners sought review of orders by the Federal Power Commission establishing new, higher gas rate ceilings which in

effect reversed, without substantial analysis, an order adopted just two months earlier. In its petition, Mobil argued, in part, that the Commission's actions were unsupported by findings of fact or substantial evidence and were therefore invalid. This Court, in affirming the agency's order, stated:

"The information before the Commission, which forms the 'record' before this court, is scant. Yet, if from this record we can determine '... that the factual predicate for the Commission's action could be a reasoned conclusion from the record as a whole ...' the Commission's action must be sustained." 152 U.S. App. D.C. at 129, 469 F.2d at 140.

While there must be a reasoned basis for agency action, informal rule-making does not require a "formal opinion covering all rejected alternatives." *Cosmetic, Toiletry and Fragrance Association, Inc., v. Schmidt*, 409 F. Supp. 57, 62 (D.D.C. 1976), citing *Consumers Union of United States, Inc. v. Consumer Product Safety Commission*, 491 F.2d 810, 812 (2d Cir. 1974). Where a concise general statement of the regulation's basis and purpose is included in the Commission's order, the agency's action is not arbitrary or capricious just because it does not include "specific and detailed findings and conclusions of the kind customarily associated with formal proceedings." *National Nutritional Foods Association v. Weinberger*, 512 F.2d 688, 700, 701 (2d Cir.), cert. denied sub nom. *National Nutritional Foods Association v. Matthews*, 423 U.S. 827 (1975).

The rule of law that agency actions taken without formal hearings need not be based on detailed findings and conclusions in the record is especially applicable where, as in this case, the agency's action is based on staff reports or other internal work product of the agency. It is clear from the transcript of the Commission's open meeting that all of the issues raised by Bradford and TAD Depository Corporation before the Commission in regard to NSCC's proposed rule

changes were analyzed in detail by the Commission's staff, and this analysis was submitted to the Commission by memorandum (A. 108, 118). But since this internal memorandum is properly confidential and therefore not part of the record,²⁰ Bradford asserts that the Commission did not specifically consider all of the relevant implications of the rule changes. Such an attempt to discredit the Commission's reasoning by reliance on the confidential nature of its internal work papers has been rejected by this Court. For example, in *Braniff Airways, Inc. v. C.A.B.*, 126 U.S. App. D.C. 399, 379 F.2d 453 (1967), which reversed the agency's ruling on other grounds, this Court ruled:

"A strong presumption of regularity supports the inference that when administrative officials purport to decide weighty issues within their domain they have conscientiously considered the issues It is well settled that even in the adjudicatory process, an administrative officer may rely on subordinates to sift and analyze the record and prepare summaries and confidential recommendations, and the officer may base his decision on these reports without reading the full manuscript The general rule remains that a party is not entitled to probe the deliberations of administrative officials, oversee their relationships with their assistants, or screen the internal documents and communications they utilize We cannot allow the recital by an administrative agency that it has considered the evidence and rendered a decision according to its responsibilities to be overcome by speculative allegations." 126 U.S. App. D.C. at 406-08, 379 F.2d at 460-62. *Accord, Flying Tiger Line, Inc., v. Boyd*, 244 F. Supp. 889, 892 (D.D.C. 1965).

This general rule is consistent with that stated by other federal circuit courts which hold that an agency may act upon

²⁰ The Act, § 23(a)(3), 15 U.S.C. § 78w(c) (1971 & Supp. 1977); Administrative Procedure Act, 5 U.S.C. § 552(b)(5) (1977).

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information contained in its own files and such internal documents, reports and deliberations are beyond the purview of contesting parties or the reviewing courts. *E.g.*, *KFC National Management Corp. v. N.L.R.B.*, 497 F.2d 298, 304-05 (2d Cir. 1974), *cert. denied*, 423 U.S. 1087 (1976); *Bank of Commerce of Laredo v. City National Bank of Laredo*, 484 F.2d 284, 287-88 (5th Cir. 1973), *cert. denied*, 416 U.S. 905 (1974); *Chrysler Corp. v. Department of Transportation*, 472 F.2d 659, 669 (6th Cir. 1972).

In the instant case, the Commission clearly set forth the reasons for its approval of the proposed rule changes and, without regard to the staff's memorandum, the "path" of the Commission's reasoning was easily discernible from the record and the prior Order granting registration. The burden is upon Bradford to show that despite the Commission's careful reasoning, there were insufficient facts to support its conclusion and that a clear error had been made. *See Maryland-National Capital Park and Planning Commission v. Lynn*, 168 U.S. App. D.C. 407, 412, 514 F.2d 829, 834 (1975); *Lewes Dairy, Inc. v. Freeman*, 401 F.2d 308, 316 (3d Cir. 1968), *cert. denied sub nom. Lewes Dairy, Inc. v. Hardin*, 394 U.S. 929 (1969). Bradford has failed completely in satisfying this burden.

CONCLUSION

The Order of the Commission dated April 21, 1977 approving NSCC's proposed rule changes should be affirmed.

Respectfully submitted,

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